

COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. NO.: 4483-01
BILL NO.: HB 2005
SUBJECT: Entertainment; Sports and Amusements; Gambling.
TYPE: Original
DATE: May 5, 2000

FISCAL SUMMARY

ESTIMATED NET EFFECT ON STATE FUNDS			
FUND AFFECTED	FY 2001	FY 2002	FY 2003
Lottery Proceeds Fund	(\$4,457,500)	(\$12,083,100)	(\$6,594,675)
Lottery Enterprise Fund	\$674,814 to Unknown	\$503,503 to Unknown	\$1,479,901 to Unknown
Higher Education Trust Fund	\$9,360,000 to Unknown	\$20,503,000 to Unknown	\$14,659,400 to Unknown
Total Estimated Net Effect on <u>All</u> State Funds	\$5,577,314 to Unknown	\$8,923,403 to Unknown	\$9,544,626 to Unknown

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2001	FY 2002	FY 2003
Total Estimated Net Effect on <u>All</u> Federal Funds	\$0	\$0	\$0

ESTIMATED NET EFFECT ON LOCAL FUNDS			
FUND AFFECTED	FY 2001	FY 2002	FY 2003
Local Government	Unknown	Unknown	Unknown

Numbers within parentheses: () indicate costs or losses
This fiscal note contains 9 pages.

FISCAL ANALYSIS

ASSUMPTION

Officials from the **Department of Revenue (DOR)** state this proposal establishes the Higher Education Trust Fund (HETF) to receive proceeds from video gaming. The fund is exempt from Section 33.080 requirements and is to be credited with its own interest. The State Treasurer is to make an annual transfer from the HETF to the Lottery Proceeds Fund equal to the reduced amount of lottery ticket sales sold pursuant to sections 313.200 to 313.350. This legislation also exempts sales tax from being charged when playing games and income tax from being imposed upon an individuals game prizes under \$600 a year.

The DOR assumes they will incur a minimal impact on processing the funds cash receipts documents. The electronic fund transfer (Section 313.403.4 page 7) should make transmittal of moneys from this legislation more convenient than manual processing requirements. The DOR assumes the exemption of sales and income taxes will not impact the Division of Taxation.

The **Missouri Lottery Commission (LOT)** did not respond to our request for fiscal impact, however, in response to similar legislation from this year that allowed video gaming machines to be placed in establishments that were licensed for the sale **and on premise consumption** of alcoholic beverages, the LOT stated this would legalize video gaming machines in Missouri. The LOT anticipated long-range sales losses for, at a minimum, the scratchers game and the pulltab game. They believed, based on their research in other states, that the pulltab game would not be able to compete in liquor-by-the-drink establishments with video gaming. The LOT assumed the pulltab game would lose approximately 25% of base sales annually for three years with an unknown reduction thereafter. Pulltab sales have increased from \$10.7 million in FY 1993 to \$29.2 million in FY 1999. This equates to a potential loss of \$7.5 million annually in gross sales in the first year.

The LOT stated that the scratchers game, if it follows the experience of South Dakota with video gaming run by the Lottery, would lose approximately 50% of its base sales annually to video gaming by the third year. The LOT estimated one-half of the sales loss experienced in South Dakota due to the fact that the games in Missouri may not be in direct competition as is the case in South Dakota convenience stores. The scratchers sales in Missouri have increased from \$115 million in FY 1993 to sales of \$248.5 million in FY 1999. The LOT assumed this equated to a potential loss of \$128.7 million in gross sales in the first three years with unknown reductions in years thereafter. Losses to the state from the decrease in sales of scratchers and pulltab games is estimated to be \$4,457,500 in FY 2001, \$16,540,600 in FY 2002, and \$23,135,275 in FY 2003

The LOT estimated that twenty-five (25) FTE would be required to administer the similar proposal. These would consist of one (1) Video Product Manager, one (1) Administrative

ASSUMPTION (continued)

Assistant, one (1) Inspector Manager, eight (8) VLT Field Inspectors, four (4) Computer Operator I's, three (3) Computer Operator II's, one (1) Communication Specialist, one (1) VLT Certifier Specialist, one (1) Systems Administrator, one (1) Programmer Analyst II, one (1) Game Accountant, one (1) Licensing Specialist II, and one (1) Security Specialist II. These positions were based upon staffing levels in the state of South Dakota and within the Missouri Lottery. Additional expenses include necessary office equipment/supplies, travel expense, consulting and research, and 6 new vehicles. Costs for a central computer system have been estimated at \$1,900,000 in FY 2001, and \$79,000 each year thereafter.

The LOT estimated the revenue from licensing fees to be \$4,775,000 in FY 2001, \$3,575,000 in FY 2002 and \$4,325,000 in FY 2003. The LOT also estimated revenues from the video lottery system as \$15,600,000 in FY 2001, \$41,600,000 in FY 2002 and \$52,000,000 in FY 2003.

The **Missouri Highway Patrol (MHP)** also did not respond to our request for fiscal impact, however, in response to similar legislation from this year that allowed video gaming machines to be placed in establishments that were licensed for the sale **and on premise consumption** of alcoholic beverages, the MHP stated that their agency would require a total of 27 FTE (25 patrolmen and 2 clerical staff) to perform background checks on prospective licensees.

Oversight assumed that most of these employees would be needed to handle the initial load of license requests. Costs should be less after the first three fiscal years. It is assumed for purposes of this fiscal note that the background checks performed by the MHP would be part of the administrative costs of the Missouri Lottery.

Officials from the **Office of Administration (OA)** assumed this would not result in any impact on Total State Revenue or any fiscal impact on their agency. However, the proposal may result in considerable general revenue fund costs. The proposal contains a provision (Sec. 313.403, subsection 6) that would help insulate the lottery proceeds fund (and programs that rely on the fund) from revenue losses resulting from the institution of video gambling as described in this proposal. However, the proposal contains no similar provision to protect the gaming proceeds for education fund (riverboat gambling) from such revenue losses. Since the types of games this bill would permit are currently available only on riverboats, it would appear that the proposal could reasonably be expected to result in a significant erosion in gaming proceeds for education fund receipts. Except for seven million dollars used for the school district bond program, all gaming proceeds for education fund revenues are used to fund the school foundation formula. The Governor recommended \$180.2 million for FY 2001 for the school foundation formula from the gaming proceeds for education fund. Any reduction in that amount would have to be replaced with general revenue funds if the school foundation formula was to remain fully funded. Likewise, the proposal could result in significant reductions in the amount of gaming

ASSUMPTION (continued)

commission fund revenue. Gaming commission fund net proceeds are the revenue source for the veteran's commission capital improvement trust fund, Missouri National Guard trust fund, Missouri college guarantee fund and the early childhood development, education and care fund. Thus, any significant downturn in gaming commission fund revenues would place the programs supported by these funds in jeopardy unless sufficient general revenue funds were available to make up the difference.

The OA also stated that Article III, Section 39(b), subsection 3 of the Missouri Constitution requires that lottery net proceeds be transferred to the lottery proceeds fund, and that monies in the fund be appropriated for public institutions of elementary, secondary and higher education. Based on that requirement, the OA questioned whether it would be constitutional to transfer revenue received by the Lottery Commission for video gaming to the higher education trust fund as required by Section 313.403, subsection 6 of this proposal.

Officials from the **Missouri Gaming Commission** state that they agree with the Office of Administration's response to this proposal.

Officials from the **Office of Secretary of State (SOS)** assume there would be costs due to additional publishing duties related to the Lottery Commission's authority to promulgate rules, regulations, and forms. SOS estimates the department could require approximately 18 new pages of regulations in the Code of State Regulations at a cost of \$26.50 per page, and 27 new pages in the Missouri Register at a cost of \$22.50 per page. Costs due to this proposal are estimated to be \$1,085. The actual fiscal impact would be dependent upon the actual rule-making authority and may be more or less. Financial impact in subsequent fiscal years would depend entirely on the number, length, and frequency of the rules filed, amended, rescinded, or withdrawn. SOS does not anticipate the need for additional staff as a result of this proposal; however, the enactment of more than one similar proposal may, in the aggregate, necessitate additional staff.

Oversight assumes the SOS could absorb the costs of printing and distributing regulations related to this proposal. If multiple bills pass which require the printing and distribution of regulations at substantial costs, the SOS could request funding through the appropriation process. Any decisions to raise fees to defray costs would likely be made in subsequent fiscal years.

Officials from the **Office of the State Courts Administrator** and the **State Treasurer's Office** assume this proposal will not fiscally impact their respective agencies.

Officials from the **Office of State Public Defender** assume they could provide representation for those 20-25 cases arising where indigent persons were charged with tampering with a video gaming machine. However passage of more than one similar bill would require the State Public

ASSUMPTION (continued)

Defender System to request increased appropriations to cover cumulative cost of representing the indigent accused in the additional cases.

Officials from the **Department of Higher Education (CBHE)** state this proposal specifies the distribution of funds out of the higher education trust fund as follows: not less than 10% for maintenance and repair at public four-year schools; not less than 5% for maintenance and repair at two-year schools; not less than 5% to fund bond major renovations and capital improvements at all public schools; not less than 5% to the Gallagher Student Grant Program; and not less than 5% to various purposes to be determined by the Governor and General Assembly. The operations of the network are funded by new fees on video gaming machine manufacturers, distributors, operators, and on video gaming machine locations. The proposal also provides various new regulations regarding video gaming machines.

The CBHE assumes there would most likely be a positive fiscal impact on higher education as a new revenue source is created for certain higher education programs.

Oversight assumes this proposal will not have a negative impact on the gaming boat revenues. Oversight also assumes the proposal will generate additional funds which will be used for specific purposes, but does not mandate new programs or costs.

Oversight assumes the similar proposal that the Missouri Highway Patrol and the Lottery Commission responded to limited the establishments that could install the electronic video gaming machines to liquor-by-the-drink consumption establishments. This proposal is much broader and incorporates any establishment licensed for the sale of alcoholic beverages, which could include grocery stores, convenient marts, liquor stores, drug stores, etc. Therefore, Oversight has expanded the fiscal impact as reported by the agencies in response to the similar legislation to incorporate the possible increase in machines.

Oversight lowered the LOT's estimates for license fee revenues and video lottery revenues to reflect a three machine maximum per premise (LOT used four machines in their estimates) and a twenty percent tax (LOT used twenty-five percent) to be paid to the state of the net revenue per machine. Oversight has assumed that the top end of the expanded spectrum would have unknown costs and generate unknown revenues. The LOT assumed there would be a total of 2,500 retailers installing 10,000 electronic video gaming machines by the end of the third year. According to the Department of Public Safety, Division of Liquor Control, 6,704 by-the-drink liquor licenses and 4,921 by-the-package liquor licenses were issued in fiscal year 1999.

Oversight assumed the estimates regarding the loss in scratchers and pulltabs revenue would not change.

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FISCAL IMPACT - State Government

FY 2001 FY 2002 FY 2003
 (10 Mo.)

LOTTERY PROCEEDS FUND

Income to Lottery Proceeds Fund

Transfer from Higher Education Trust Fund	\$0	\$4,457,500	\$16,540,600
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Loss to Lottery Proceeds Fund

Reduction in instant lottery revenues due to video lottery	(\$4,457,500)	(\$16,540,600)	(\$23,135,275)
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NET EFFECT TO LOTTERY PROCEEDS FUND

(\$4,457,500) (\$12,083,100) (\$6,594,675)

LOTTERY ENTERPRISE FUND

Income - Licensing Fees

\$4,400,000	\$3,075,000	\$3,700,000
to unknown	to unknown	to unknown

Costs - to the Lottery Commission

Personal Service (at least 25 FTE)	(\$465,322	(\$620,429	(\$651,451
	to unknown)	to unknown)	to unknown)

Fringe Benefits	(\$143,087	(\$190,782	(\$200,321
	to unknown)	to unknown)	to unknown)

Expense and Equipment	(\$2,302,500	(\$354,000	(\$354,000
	to unknown)	to unknown)	to unknown)

Total <u>Costs</u> to the Lottery Commission	(\$2,910,909	(\$1,165,211	(\$1,205,772
	To Unknown)	To Unknown)	To Unknown)

Costs - to the Missouri Highway Patrol

Personal Service (at least 27 FTE)	(\$548,744	(\$674,955	(\$691,829
	to unknown)	to unknown)	to unknown)

Fringe Benefits	(\$210,608	(\$259,048	(\$265,524
	to unknown)	to unknown)	to unknown)

Expense and Equipment	(\$54,925	(\$472,283	(\$56,974
	to unknown)	to unknown)	to unknown)

Total Costs to the Missouri Highway Patrol	(\$814,277	(\$1,406,286	(\$1,014,327
	To Unknown)	To Unknown)	To Unknown)

NET EFFECT TO THE LOTTERY ENTERPRISE FUND

\$674,814 \$503,503 \$1,479,901
To Unknown To Unknown To Unknown

<u>FISCAL IMPACT - State Government</u>	FY 2001	FY 2002	FY 2003
(continued)	(10 Mo.)		

HIGHER EDUCATION TRUST FUND

<u>Income</u> - Video lottery revenues	\$9,360,000	\$24,960,000	\$31,200,000
	to unknown	to unknown	to unknown
<u>Costs</u> - Transfer to Lottery Proceeds Fund	\$0	(\$4,457,000)	(\$16,540,600)

NET EFFECT ON HIGHER EDUCATION TRUST FUND	\$9,360,000	\$20,503,000	\$14,659,400
	<u>To Unknown</u>	<u>To Unknown</u>	<u>To Unknown</u>

<u>FISCAL IMPACT - Local Government</u>	FY 2001	FY 2002	FY 2003
	(10 Mo.)		

<u>Income</u> - Appropriations for specific higher education purposes	unknown	unknown	unknown
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A portion of the appropriations from the Higher Education Trust Fund would go to the Local Public Community Colleges.

FISCAL IMPACT - Small Business

A fiscal impact to small businesses qualified to host video gaming machines would be expected as a result of this proposal.

DESCRIPTION

This proposal authorizes the Missouri Lottery Commission to establish a video gaming machine network. The system will be operated and audited through a central computer communications system, dedicated to the operation of the network. All revenue generated by the network will be deposited into the Higher Education Trust Fund, created by the proposal. The money will be appropriated as follows:

- (1) At least 10% for maintenance, repair, and major renovation of buildings constructed with state funds on public 4-year institutions of higher education, not to exceed 1.5% of the

DESCRIPTION (continued)

replacement cost of the buildings;

(2) At least 5% to community colleges for maintenance and repair of facilities, not to exceed 1.5% of the replacement cost of the facilities;

(3) At least 5% to fund bonds to be issued for major renovations and new capital improvement projects at public 4--year institutions of higher education and community colleges;

(4) At least 5% to the student grant program, not to exceed the amount necessary to fund fully the program so that all qualified students may receive the prescribed amount; and

(5) At least 5% for other state scholarship programs, higher education research programs, endowed chairs, any other higher education purpose deemed appropriate by the General Assembly and the Governor, and administrative costs incurred by the Department of Higher Education.

Application and licensing fees for video gaming machine manufacturers, distributors, and operators are established. The fees will pay for the administrative expenses of the commission in administering the network. A license will not be granted to any person who has been convicted of a felony, and the commission may deny a license to anyone convicted of a gambling--related offense.

The proposal establishes video gaming machine requirements and requirements for video gaming machine operators licensed by the commission. The directory will contract with licensed operators for one year at a time. No one under 21 years of age is authorized to play a licensed video gaming machine. Tampering with a licensed machine with intent to interfere with the proper operation of the machine or manipulate the outcome or payoff is a class D felony. Operation of a gray area device, as defined in the proposal, after the effective date of the proposal, for use by members of the public is a class D felony.

This legislation is not federally mandated, would not duplicate any other program, but may, however, require additional capital improvements or rental space to house the additional FTE requested by the Lottery Commission or the Highway Patrol or the Lottery Commission's mainframe computer.

SOURCES OF INFORMATION

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Department of Revenue
Missouri Gaming Commission
Department of Higher Education
Department of Public Safety
Division of Liquor Control
Office of the Secretary of State
Office of the State Treasurer
Office of the State Courts Administrator
Office of the State Public Defender
Department of Corrections

NOT RESPONDING: **Missouri Lottery Commission**
 Missouri Highway Patrol

A handwritten signature in black ink, appearing to read "Jeanne Jarrett". The signature is stylized with a large, looped initial "J" and a cursive script.

Jeanne Jarrett, CPA
Director
May 5, 2000